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Defending the "Time Culture": The Public and Private Interests of Media Corporations

Shelby D. Green
Elisabeth Haub School of Law at Pace University

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INTRODUCTION

Since the daring attempt in 1985 by Turner Broadcasting System to capture CBS,[1] there has not been a more exciting contest of media giants than the recent one between Time, Inc. ("Time") and Paramount Communications, Inc.[2] The contest is

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* Associate Professor of Law, Pace University; J.D. 1980, Georgetown University Law Center; B.S. 1976, Towson State University.

1. "CBS" is the acronym for Columbia Broadcasting Systems, a television network and a licensee of radio and television stations.

2. Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1989). Over the years, in addition to its magazines (*Time*, *People*, *Sports Illustrated*), Time has dabbled in newspapers, movie production, forest products and TV stations.

At the time of the contest, Time also owned substantial cable interests—American Television & Communications Corporation, HBO and Cinemax. In addition, Warner Communications, Inc. ("Warner") and Time held significant ownership positions in Turner Broadcasting (which owns Cable News Network ("CNN"), Superstation WTBS, a broadcast licensee, and Turner Network Television) and together would control 17% of Turner. Answering Brief of Defendant-Appellee Warner Communifamous not simply for the shrewd takeover strategies employed (both offensively and defensively) but also for the novel, yet bold, grounds asserted by Time in defense against the takeover. Time's board of directors proclaimed its duty and privilege to fend off Paramount to protect the "Time Culture"—this notion that Time had become recognized in this country as an institution built upon a foundation of journalistic integrity.[3]

The full import of the "Time Culture" is not clear. It may mean nothing more than a belief that high quality work will engender audience loyalty and, therefore, continued financial success. On the other hand, the "Time Culture" may be a recognition by the board of directors of additional, societal responsibilities owed by an influential media corporation—"an enterprise operated in the public interest."[4]

The Federal Communications Act 1934, ("the Act")[5] requires licensees and franchisees to serve the "public interest, convenience and necessity" in exchange for the privilege of using the broadcast spectrum.[6] The fact that many such operators, like those controlled by Time, are organized as corporations may seem to create a conflict, because, traditionally, the business corporation's only legitimate interest is the "business interest" of making a profit.[7] While the traditional view has changed some-

cations, Inc. at 5, *Paramount Communications, Inc.*, 571 A.2d 1140 (No. 279). Warner also owned, among other things, a major film studio and had begun to expand into the business of television program production—having just entered into a merger agreement to acquire Lorimar Telepictures, an important producer of television programs. Brief of Defendant Warner Communications, Inc. in Opposition to Motions for a Preliminary Injunction at 17, 571 A.2d 1140 (C.A. No. 10,670).

3. Time Defendants' Brief in Opposition to Plaintiff's Motions for a Preliminary Injunction at 15-16, *Paramount Communications, Inc.*, 571 A.2d 1140 (C.A. No. 10,670). These "same tenets" of Time's corporate culture "have been extended to the rest of Time, Inc.'s book business" and the "same philosophy pervades . . . [the] cable business." *Id.* at 16 n.7.

4. *Id.* at 34 (statement of Henry Luce, III, Outside Director, Time). Of course, as to its magazine operations, Time always has been free to ignore any non-traditional business concern in its editorial decisions. Indeed, to ensure that the editorial side of the company would operate free from intrusion by the business side, the company separated these functions by creating a "church-state" structure. *Id.* at 16.

5. Federal Communications Act of 1934, 47 U.S.C. §§ 151-612 (1988).

6. *Id.* § 309(a) (1988).

7. Dodge v. Ford Motor Co., 204 Mich. 459, 507, 170 N.W. 668, 684 (1919) ("A business corporation is organized and carried on primarily for the profit of the stockholders"); *see also* Green, *Corporate Philanthropy and the Business Benefit: The Need for Clarity*, 20 GOLDEN GATE U.L. REV. 239 (1990) (even though many corporations

what,[8] corporate directors must still have profitability as their central focus. At the same time, by the language of the Act, corporate broadcast licensees have additional and special obligations. They must also serve the "public interest."

While the notion of the "Time Culture" is discussed in detail below, by way of introduction, a few questions seem pertinent. If the "Time Culture" means that a media corporation may have additional societal responsibilities, this raises significant corporate law issues: when are directors of business corporations, in particular media corporations, permitted to consider any object other than shareholder wealth maximization? Should the range of legitimate factors for decisionmaking be broader for media corporations, particularly those regulated by the Federal Communications Commission ("FCC" or "Commission")? If so, and these corporations must consider the public interest, how does the corporate broadcaster discover and satisfy it, and how should a corporation reconcile the conflict between maximizing profits and serving the public interest? When will a choice in favor of the public interest be upheld under traditional corporation doctrine?

Part I of this essay discusses the "public interest" standard under the Federal Communications Act and describes parallels in corporation doctrine. Part II considers whether broadcasters satisfy their public interest obligations by addressing audience interest. Part III discusses the prerogatives of the management

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do engage in philanthropic activities, their primary motivation may be long run economic benefit).

8. *See* A.P. Smith Mfg. Co. v. Barlow, 13 N.J. 145, 154, 98 A.2d 581, 586 ("[M]odern conditions require that corporations acknowledge and discharge social, as well as private, responsibilities as members of the communities within which they operate"), *appeal dismissed*, 346 U.S. 861 (1953).

The American Law Institute has suggested that:

> A business corporation should have as its objective the conduct of business activities with a view to enhancing corporate profit and shareholder gain, except that, whether or not corporate profit and shareholder gain are thereby enhanced, the corporation, in the conduct of its business . . . .
>
> . . . .
>
> (b) may take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business. . . .

PRINCIPLES OF CORPORATE GOVERNANCE § 2.10 (Tent. Draft No. 2, 1984). In the Comment to this section, the ALI explains that the "ethical considerations" referred to include "an orientation toward lawful, ethical, and public-spirited activity." *Id.* at comment f.

of the corporate broadcaster to consider non-financial factors in selecting programming. Part IV describes the non-traditional philosophy of the corporation's legitimate object, which led to the subject case. Part V discusses the central legal issues of the cognizable business interests of corporations. Finally, the Conclusion offers a view on desirable public interest objectives of media corporations.

I. "PUBLIC INTEREST" UNDER THE FEDERAL COMMUNICATIONS ACT

"[P]ublic interest, convenience and necessity" are not defined in the Act[9] and courts and the Commission have labored since its passage to determine what Congress meant by these words. The language of the Act gives the Commission no specific supervisory control of programs, business management, or policy. Yet in the fifty years following its enactment, the Commission has adopted rules and policies to do just that, determining that the public interest required them.[10] For example, the

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9. The Act does authorize the Commission, in furtherance of these ends, to "study new uses for radio . . . and generally encourage the larger and more effective use of radio." 47 U.S.C. § 303(g) (1988). The Act also requires the FCC to provide a "fair, efficient and equitable distribution of radio service." *Id.* at § 307(b) (1988).

10. Indeed, this theory of regulation began under the Act's predecessor, the Federal Radio Act of 1927. The Federal Radio Commission, created by the Radio Act of 1927, required licensees to: file program schedules; explain how the operation of the station would serve the public interest, convenience, and necessity; and state the average amount of time weekly devoted to entertainment, religious, commercial, educational, agricultural and fraternal programs. The Federal Radio Commission further decided that well-rounded program service should include "entertainment, religion, education, and instruction, important public events, discussion of public questions, weather, market reports, and news and matters of interest to all members of the family." F. KAHN, DOCUMENTS OF AMERICAN BROADCASTING 150-51 (3d ed. 1978) (providing a thorough discussion of the history of the Federal Radio Commission's regulatory theory). *See also* Note, *Changing Channels in Broadcast Regulation: Leaving Television Advertising to Containment by Market Forces*, 34 CASE W. RES. 465 (1984) (discussing history of FCC regulatory theory as part of an analysis of recent changes in the theories currently espoused by the FCC); FCC, PUBLIC SERVICE RESPONSIBILITY OF BROADCAST LICENSEES (1946) (the "Blue Book").

Later, the FCC developed a framework for the comparative evaluation of broadcast applicants in Policy Statement on Comparative Broadcast Hearings, 1 F.C.C.2d 393, 5 R.R.2d 1901 (1965). There, the Commission enunciated two primary objectives—to provide: (1) the best practicable service to the public; and (2) diversification of control of the mass communications media. In implementing these objectives, the FCC deemed important the full-time owner participation in station operations and considered the past broadcast record of applicants and their moral character. *Id.* at

Commission at one time determined that it was in the public interest to require licensees to ascertain community issues and offer programming addressing those needs.[11] It was determined to be in the public interest to limit the number of commercials aired during children's programs.[12] In addition, the Commis-

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395, 5 R.R.2d at 1904. The FCC considered the proposed program service most important, and required that an "applicant have the responsibility for a reasonable knowledge of the community and area, based on surveys or background, which will show that the program proposals are designed to meet the needs and interests of the public in that area." *Id.* at 397, 5 R.R.2d at 1905.

To ensure attention to the needs of minority populations, the FCC also required licensees to adopt equal employment opportunity programs. 47 C.F.R. § 73.2080 (1990).

11. Network Programming Inquiry, Report and Statement of Policy, 20 R.R. 1901 (1960) (en banc); *see also* Community Problems—Broadcast Applicants, 27 F.C.C.2d 650, 21 R.R.2d 1507 (1971) (setting forth guidelines for broadcast applicants in ascertaining community problems). The FCC required all applicants for new broadcast stations, modification of existing facilities and renewals to determine the economic, ethnic and social composition of the communities they proposed to serve and to consult with leaders from each significant community group to ascertain the programming needs and interests of the entire community. The FCC then required the applicant to set forth in its license application specific program proposals designed to meet the identified community needs. A licensee that failed to properly address these needs risked non-renewal. Alabama Educ. Television Comm'n ("AETC"), 50 F.C.C.2d 461, 32 R.R.2d 539 (1975).

In denying renewal in *Alabama Educational Television Commission*, the FCC found that "blacks rarely appeared on AETC programs; that no black instructors were employed in connection with locally-produced in-school programs; and that unexplained decisions or inconsistently applied policies forced the preemption of almost all black-oriented network programming." *Id.* at 469, 32 R.R.2d at 556. The FCC ruled that the AETC "followed a racially discriminatory policy in its overall programming practices and, by reason of its pervasive neglect of a black minority consisting of approximately 30 percent of the population of Alabama, its programming did not adequately meet the needs of the public it was licensed to serve." *Id.* at 477, 32 R.R.2d at 555. The FCC went on to say that a licensee "cannot with impunity ignore the problems of significant minorities in its service area." *Id.* at 473, 32 R.R.2d at 551.

12. Action for Children's Television, 50 F.C.C.2d 1, 11, 31 R.R.2d 1228, 1240 (1974), *aff'd*, 564 F.2d 458 (D.C. Cir. 1977). The FCC had strived to ensure that children's television programming and advertising reflected the "high public interest considerations involved in the use of television, perhaps the most powerful communications medium ever devised, in relation to a large and important segment of the audience, the nation's children." Children's Programs, 28 F.C.C.2d 368, 369-70 (1971). In *Action for Children's Television*, the FCC concluded that: (1) because of their youth and inexperience, "children are far more trusting of and vulnerable to commercial 'pitches' than adults"; and (2) "very young children cannot distinguish conceptually between programming and advertising." 50 F.C.C.2d at 11, 31 R.R.2d at 1240.

The FCC declined to adopt specific guidelines on the permissible level of advertising in children's programming. However, the FCC endorsed the restrictions adopted by the industry—that there should be no more than nine and a half minutes per hour sion determined and the Supreme Court agreed that the public interest required licensees to air issues that "are so critical and of such great importance that it would be unreasonable for a licensee to ignore completely" and also to require that if a broadcaster covered a "controversial issue of public importance, it was required to take steps to assure that significant contrasting views are also presented": the Fairness Doctrine.[13]

But the sway of the Commission on its notion of the public interest proved as variable as the political winds. The Fairness Doctrine is a case in point. In 1970, the Commission described the Fairness Doctrine "as the single most important requirement of the operation in the public interest — the *sine qua non* for the grant of a renewal of license."[14] In 1985, after fifty years of such lofty pronouncements, the Commission discovered that the doctrine no longer encouraged the airing of controversial and opposing ideas (which surely serves the public interest) but indeed worked to inhibit the communication of ideas.[15] The Commis-

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on weekdays and twelve minutes per hour on weekends devoted to non-program material, and that broadcasters should strictly maintain adequate separation between program content and commercial messages. The FCC stated that compliance with the industry guidelines would be sufficient to resolve in favor of the station any questions as to whether its commercial practices serve the public interest, and licensees who exceed these levels should be prepared to justify their advertising policy. *Id.* at 14, 31 R.R.2d at 1242.

In November 1990, President Bush signed into law The Children's Television Act of 1990, Pub. L. No. 101-437, 104 Stat. 996 (1990). Among other things, this Act limits commercials during children's television programs to no more than 12 minutes per hour on weekdays and 10 and a half minutes on weekends.

13. Red Lion Broadcasting Co. v. FCC, 396 U.S. 367 (1969); NBC v. United States, 319 U.S. 190 (1943). As for cable television, the Act establishes procedures and standards which "assure that cable systems are responsive to the needs and interests of the local community." 47 U.S.C. § 521(2) (1988).

14. Fairness Doctrine Ruling, 25 F.C.C.2d 283, 292, 19 R.R.2d 1103, 1111 (1970).

15. Fairness Doctrine, 102 F.C.C.2d 143, 58 R.R.2d 1137 (1985). To the question of how the expression of ideas is suppressed if broadcasters are *required* to offer discussion of important issues, the broadcasters countered with the argument (perhaps more ingenious than convincing) that, in order to avoid the economic burdens of having to make available free air time for the other side of a controversial issue, they would avoid the airing of important issues in the first place. This liberal reading of the Fairness Doctrine would allow broadcasters to impose their economic interests in place of the "public interest" under the Act. However, this argument runs contrary to the Supreme Court's view that "[i]t is the right of the viewers and listeners, not the right of the broadcasters, which is paramount." Red Lion Broadcasting Co. v. FCC, 396 U.S. 367, 390 (1969). Also, this argument depends upon a more flexible interpretation of the first prong of the Fairness Doctrine than the language suggests.

sion repealed the Fairness Doctrine and, with the deregulation of broadcasting generally (including those provisions eliminating ascertainment requirements, lifting restrictions on commercials, and dropping guidelines for public service, news and non-entertainment programs[16]), no longer would a broadcaster need to be concerned about societal or community issues.[17] In accordance with Commission regulations, the only forces that remained to move broadcasters were market forces.[18]

This idea that those receiving special privileges from government should in some way serve the public interest also describes early corporate law.[19] Professor Hurst teaches that the granting of special privileges, such as to "establish rights of way and charge tolls or to issue banknotes or to exercise the power of eminent domain" (the usual work of the early corporations) were "reconciled with our egalitarian conscience, first, by insisting that government's action . . . be legitimated by determining that it was in the public interest to confer special privileges to obtain services for public convenience or necessity."[20] Further, the government attached limiting standards or rules to the special privileges to protect those who would become dependent on the fairness and quality of the service the corporation would pro-

16. Commercial TV Stations, 98 F.C.C.2d 1076, 56 R.R.2d 1005 (1984); Deregulation of Radio, 84 F.C.C.2d 968, 49 R.R.2d 1 (1981). After court challenges, the FCC modified its position to require licensees to maintain a list of programs that have provided the station's most significant treatment of community issues during the preceding three-month period. However, there are no specific, affirmative requirements to offer any such programs. Deregulation of Radio, 104 F.C.C.2d 505, 507, 60 R.R.2d 789, 790 (1986).

17. *See* Simon Geller, 102 F.C.C.2d 1443, 59 R.R.2d 579 (1985) (FCC renewed license when licensee had presented no programming whatsoever on community issues). A broadcaster who has failed to deliver any non-entertainment programming, though, risks losing a "renewal expectancy." A renewal expectancy is a preference given to an incumbent licensee who demonstrates that its past program service has been meritorious in meeting the needs and interests of listeners or viewers in its license or service area. The value of the preference will vary depending upon the licensee's record and even may be decisive where the licensee's past record is found to be "superior," such as where there has been an unusually high attention to community needs and interests. Central Fla. Enters. v. FCC, 683 F.2d 503, 506 (D.C. Cir. 1982), *cert. denied*, 460 U.S. 1084 (1983).

18. *See* Fowler & Brenner, *A Marketplace Approach to Broadcast Regulation*, 60 TEX. L. REV. 207 (1982) (arguing that the FCC should amend its model of broadcast regulation to account for market forces).

19. J. HURST, THE LEGITIMACY OF THE BUSINESS CORPORATION IN THE LAW OF THE UNITED STATES: 1780-1970, at 60 (1970).

20. *Id.*

vide.[21] Since important special-action franchises were stated in corporate charters, it seemed natural to enforce responsibility upon these corporations by regulating their business organizations, as well as their business.[22] Hurst explains that "[b]y the mid-nineteenth century various regulatory provisions, such as limits on capitalization . . . became common in special corporate charters."[23] Not until the great momentum of the industrial revolution did states loosen their hold upon the activities of business corporations on the view that the "corporate instrument was so useful for desired economic growth as to warrant using law to make it available on terms most responsive to businessmen's needs or wishes."[24]

The mid-nineteenth century liberalization of corporation statutes with the consequent privatization of corporate affairs fostered the view that corporations had no public service obligations. Soon it became the dominant theory that any objective other than to maximize shareholder wealth was *ultra vires* ("beyond powers") and therefore illegal.[25]

However, nearly a century later, corporate law scholars and legislators were no less reluctant than the Commission to rethink the concept of the corporation in light of economic, political and historical developments. They seem willing to afford directors discretion to expand the range of permissible considerations in corporate decisionmaking. Arguably, the circle is complete with the enactment of statutes permitting directors to consider groups other than shareholders, such as employees, suppliers and the community in making business decisions.[26]

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21. *Id.*

22. *Id.* at 60-61. Restrictions also were imposed on corporate size and scope of activity. *Id.* at 61.

23. *Id.*

24. *Id.* at 62; *see also* Seavoy, *The Public Service Origins of the American Business Corporation*, 52 BUS. HIST. REV. 30 (1978) (noting that the test of importance to the general welfare, originally confined to municipal or benevolent enterprises, was being applied to manufacturing ventures by the second decade of the nineteenth century).

25. Dodge v. Ford Motor Co., 204 Mich. 459, 507, 170 N.W. 668, 684; J. HURST, *supra* note 19, at 69-71.

26. For example, the Massachusetts business corporation statute provides:

> In determining what he reasonably believes to be in the best interests of the corporation, a director may consider the interests of the corporation's employees, suppliers, creditors and customers, the economy of the state, region and nation, community and societal considerations, and the long-term and short-term interests of the corporation and its stockholders, including the

II. THE PUBLIC INTEREST AND AUDIENCE INTEREST

While the deregulation of radio and television removed many burdens from broadcasters (largely leaving market forces to determine the program policies), a few restrictions were retained. Some of these remaining regulations reflect the belief that the public interest is served by forbidding certain kinds of broadcasts because they threaten audiences with undesirable and harmful ideas and values. This public interest, thus, demands that radio and television not broadcast indecent or obscene material,[27] distortion of the news,[28] advertisements of lottery information[29] or cigarette commercials.[30]

> possibility that these interests may be best served by the continued independence of the corporation.

MASS. GEN. L. ch. 156B, § 65 (1990). Pennsylvania was the first state to adopt a statute that specifically authorized directors to consider the interests of groups other than shareholders in making decisions. 15 PA. CONS. STAT. ANN. § 1721(c) (Purdon 1990). Since then, many other states have enacted similar laws. *See, e.g.*, ARIZ. REV. STAT. ANN. § 10-1202 (1989), CONN. GEN. STAT. § 33-313(e) (1990), FLA. STAT. § 607.0830(3) (1989), GA. CODE ANN. § 14-2-202(b)(5) (1990), HAW. REV. STAT. § 415-35(b) (1990), IDAHO CODE §§ 30-1602, 30-1702 (1990), ILL. ANN. STAT. ch. 32, para. 8.85 (Smith-Hurd Supp. 1990), IND. CODE ANN. § 23-1-35-1(d) (Burns 1989), KY. REV. STAT. ANN. § 271B.12-210 (Michie/Bobbs-Merrill 1990), ME. REV. STAT. ANN. tit. 13-A § 716 (1989), MINN. STAT. § 302A.251 (1990), NEB. REV. STAT. § 21-2035 (1989), N.M. STAT. ANN. § 53-11-35 (1978 & Supp. 1989), N.Y. BUS. CORP. LAW § 717 (Consol. 1991), OHIO REV. CODE ANN. § 1701.59(E) (Baldwin 1990), S.D. CODIFIED LAWS ANN. § 47-33-4 (1990).

27. Under federal law, it is unlawful to broadcast obscene or indecent matter. 18 U.S.C. § 1464 (1988). In April 1987, the FCC issued new indecency standards which prohibited the broadcast of indecent matter during hours when there is a reasonable risk that the audience may consist of children. New Indecency Enforcement Standards to be Applied to All Broadcast and Amateur Radio Licensees, 2 FCC Rcd 2726 (1987). Broadcasters challenged these standards on vagueness grounds. Action for Children's Television v. FCC, 852 F.2d 1332 (D.C. Cir. 1988). The D.C. Circuit Court remanded the case with the direction that the FCC adopt a workable definition of indecency, as well as a safe harbor for airing such programs.

In 1988, Congress passed a requirement that the FCC enforce its anti-indecency policy 24 hours a day. The FCC adopted such a policy but was precluded from enforcing it by a stay issued by the D.C. Court of Appeals. Action for Children's Television v. FCC, No. 1916, slip op. (D.C. Cir. Sept. 13, 1989).

In the area of cable television, see 47 U.S.C. § 559 (1988) (providing sanctions for the transmission "over any cable system [of] any matter which is obscene or otherwise unprotected by the Constitution") and 47 U.S.C. § 544(d)(1) (1988) (authorizing franchising authorities to prohibit and/or regulate obscene or otherwise unprotected communications).

28. Galloway v. FCC, 778 F.2d 16 (D.C. Cir. 1985).

29. 18 U.S.C. § 1304 (1988).

30. 15 U.S.C. § 1335 (1988).

These limited restrictions seem to leave many programming choices. Since deregulation, however, broadcasters have been most pedestrian and guided largely by program ratings, causing the program fare to suffer from sameness.[31] From the broadcasters' financial perspective, a programming strategy based primarily on ratings seems to work, and it follows that attention to audience interest seems to be an objective of the broadcasting business. This statement, of course, assumes that audience interest and the public interest are synonymous concepts. In fact, audiences may have interests as diverse as the population, although the ratings may not reflect this diversity because of practical and empirical flaws in the surveying techniques.[32]

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31. For the Fall 1990 television season, comedy dominated prime-time. The three networks and Fox Broadcasting offered 20 new comedy shows, adding to schedules already crowded with situation comedies. Of the 93 entertainment programs (not counting news, sports or movies) in prime-time, 50 were comedies. NBC aired a record 16 half-hour comedy shows. ABC aired 14, and Fox and CBS each aired 10. Carter, *For Networks, the Punch Line is a Bigger Bottom Line,* N.Y. Times, July 16, 1990, at D6, col 1. It seems then that the situation-comedy reigns, since this type of program received the highest ratings last season. *NBC Squeaks by CBS to Another Sweeps Win*, BROADCASTING, May 28, 1990, at 32.

The decline in program variety began in the mid-1960s when the networks switched from 30-minute programs that had dominated the prime-time schedule during the 1950s to the 60-minute format, with the exception of the situation-comedy. Starting in 1971, the three networks began to concentrate on just three formats: situation comedies, crime dramas and movies. Since that year, these three program types have filled an average of 59% of all prime-time. S. EASTMAN, S. HEAD & L. KLEIN, BROADCAST/CABLE PROGRAMMING STRATEGIES AND PRACTICES 143 (2d ed.1985) [hereinafter EASTMAN]. *See also* Atkins & Litman, *Network TV Programming: Economics, Audiences, and the Ratings Game, 1971-1986*, 36 J. COMM. 32-35 (1986) (pointing out that networks act in a uniform and interdependent manner in the area of programming; that coordinated profit-maximizing conduct has produced an increase in homogeneity and a decrease in diversity among program formats; and that while schedule manipulation and political factors are variables which may affect the ratings game and produce a different relationship, profit and loss considerations play a central role and are the primary explanatory factors in program renewals); McDonald & Achecter, *Audience Role in the Evolution of Fictional Television Content*, 32 J. BROADCASTING & ELECTRONIC MEDIA 66-71 (1988) (the authors conducted an empirical study which examined audience ratings as a component of the feedback processes in the evolution of program types and found strong relationships between audience ratings and the number of programs of a given type subsequently aired).

32. Recent reports show network concerns over flaws in the Nielsen ratings system. Among other things, the rate of cooperation by potential participants may distort the random nature that the system needs in order to represent accurately an entire nation's viewing. Viewers who agree to use the "people meter" may have systematically different television habits from those who refuse. Kneale, *TV's Nielsen Ratings, Long Unquestioned, Face Tough Challenges*, Wall St. J., July 19, 1990, at A1, col. 6;

Beyond the problems with accuracy and scientific significance, a larger problem exists with a decisionmaking process based simply on the highest ratings. This system is not calculated toward a fair assessment of larger audience concerns. Admittedly, licensees must also contend with their program advertisers who rationally choose to advertise during popular shows with high viewership. Herman and Chomsky argue that the power of advertisers over television programming stems from the simple fact that they are the "patrons" who provide the media subsidy: "the media compete for their patronage, developing specialized staff to solicit advertisers and necessarily having to explain how their programs serve advertisers' needs."[33]

These advertisers then become "normative reference organizations," whose requirements and demands the media must

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see also Nielsen Peoplemeters Get Two-Year Network Review, BROADCASTING, Dec. 18, 1989, at 68 (ABC, NBC and CBS sponsored a study which found major tabulation errors for larger households and those with cable); *NAB, Networks Call for Study of Peoplemeters*, BROADCASTING, Mar. 21, 1988, at 27 (networks charged there were biases in sample groups and that some family members, particularly young children, were not properly registering their viewing).

Even broadcasters, whose advertising dollars have ebbed because of reportedly low viewership, have challenged the accuracy of audience surveys. New studies contend that the Nielsen ratings significantly understate viewing in a number of ways, especially by children and young adults and by people in bars, hotels and on vacation. In general, the accuracy of the ratings depends upon the faithfulness of the viewers in logging their program choices. Studies show that viewers often: (1) forget or neglect to activate the monitoring device (the people meter); (2) log in, but do not watch the program; or (3) are too young to report viewing accurately (e.g., tots watching Saturday morning cartoons). Then there is the problem of obtaining a sample of households sufficient to produce statistically significant results. In fact, almost half of homes contacted by Nielsen refuse to join its people meter sample, and only 47% stay on as members of the Nielsen system. A recent phone survey of 26,000 homes indicated that 26% more men aged 18 to 34 and 33% more kids watched TV than Nielsen showed for the same period. The phone survey also showed 52% more visitors watched television in other people's homes than Nielsen reported. Kneale, *TV's Nielsen Ratings, Long Unquestioned, Fact Tough Challenges*, Wall St. J., July 19, 1990, at A1, col. 6; *see also Nielsen Study Finds 6.3 Million Uncounted Viewers*, BROADCASTING, May 14, 1990, at 40.

33. E. HERMAN & N. CHOMSKY, MANUFACTURING CONSENT: THE POLITICAL ECONOMY OF THE MASS MEDIA 16 (1988) [hereinafter HERMAN & CHOMSKY]. The authors sketch a "propaganda model" and apply it to the performance of the mass media in the United States. They provide a critical analysis of the media's coverage of several prominent national and world events, such as the strife in El Salvador, Guatemala and Nicaragua, Third World elections, the KGB-Bulgarian plot to kill the Pope, Indochina Wars, and the murders of Jerzy Popieluszko and Archbishop Oscar Romero.

accommodate in order to succeed.[34] They impose their will through the withdrawal and cancellation of advertisements on politically sensitive or unfavorable programs.[35] Herman and Chomsky state:

> Television networks learn over time that such programs will not sell

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34. *Id.* "For a television network, an audience gain or loss of one percentage point in the Nielsen ratings translates into a change in advertising revenue of from $80 to $100 million a year, with some variation depending on measures of audience 'quality.'" *Id.*

35. In May 1990, Proctor & Gamble Co., parent company of Folgers Coffee Co. and one of the biggest advertisers in television, canceled $70,000 worth of ads for all its products from CBS affiliate WHDH-TV in Boston because the station aired a commercial protesting Folgers' use of coffee beans grown in El Salvador. Proctor & Gamble spent about $1 million annually in advertising at WHDH-TV. *Proctor & Gamble Pulls TV Ads Over Slur to Coffee*, N.Y. Times, May 12, 1990, at 1. The offending commercial was produced by Neighbor-to-Neighbor, a grassroots organization working to change policy in Central America. The commercial was offered to stations in Cincinnati, New Orleans, Kansas City and Boston. WHDH-TV was the only station to air the commercial.

One "reality based" program presenting too much controversy for advertisers' comfort was the NBC airing of "Roe v. Wade," a made-for-TV movie based on the 1973 U.S. Supreme Court decision. Several advertisers withdrew commercial time fearing potential boycotts by groups who disapproved of the program's content. The network nonetheless aired the program, stating that the show did not advocate a particular viewpoint, but instead represented both positions. *Wright Defends 'Roe' to Advertisers*, BROADCASTING, May 15, 1989, at 31.

ABC reported that it lost more than $14 million because advertisers pulled commercial spots from prime-time programs those advertisers perceived as too controversial. The network lost $1 million after promoters backed away from an episode of "thirtysomething" which showed two gay men talking in bed. Advertisers also pulled ads from an episode of "Roseanne" which dealt with teenage drinking. *Igor Chastises Sponsors for Leaping Before Looking*, BROADCASTING, July 30, 1990, at 53.

In 1985, public television station WNET lost its corporate funding from Gulf & Western Industries, Inc. after the station showed a documentary, "Hungry for Profit," which contained material critical of multinational corporate activities in the Third World. The chief executive of Gulf & Western complained that the program was "virulently anti-business if not anti-American." HERMAN & CHOMSKY, *supra* note 33, at 17. Herman and Chomsky state:

> Large corporate advertisers on television will rarely sponsor programs that engage in serious criticisms of corporate activities, such as the problem of environmental degradation, the workings of the military-industrial complex, or corporate support of and benefits from Third World tyrannies . . . .
>
> . . . .
>
> Advertisers will want . . . to avoid programs with serious complexities and disturbing controversies that interfere with the "buying mood." They seek programs that will lightly entertain and thus fit in with the spirit of the primary purpose of program purchases—the dissemination of a selling message. . . . [They] will usually not want to sponsor close examinations of sensitive and divisive issues . . . .

Id.

> and would have to be carried at a financial sacrifice, and that, in addition, they may offend powerful advertisers. . . .With the rise in the price of advertising spots, the forgone revenue increases; and with increasing market pressure for financial performance and the diminishing constraints from regulation, an advertising-based media system will gradually increase advertising time and marginalize or eliminate altogether programming that has significant public-affairs content.[36]

Despite these concerns with power and control by advertisers, corporate broadcasters must have some basis on which to make assessments about programs. Nevertheless, this concern does not validate the exclusive use of audience ratings. Broadcasters may just as well survey educators, community leaders and public interest organizations to learn of audience interests. Under the existing practice, however, ratings which determine advertising volume and prices, determine the commercial success of the broadcaster, which in turn, determines program choices. While it is difficult to counter the argument that prosperous corporations, including those that are broadcast licensees, do not serve any public ends, it is another matter to say that this should be the only philosophy to judge the choices and operations of corporate broadcasters. The Act must have been intended for something loftier than pumping ratings.[37] This idea

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36. HERMAN & CHOMSKY, *supra* note 33, at 17; *see also* B. OWEN, J. BEEBE, W. MANNING & W. WILLARD, TELEVISION ECONOMICS 101 (1974); Atkins & Litman, *supra* note 31, at 32-33 (presenting a model to ascertain the "critical mass" in ratings points required to facilitate renewal of prime-time network programs and maintaining that a network will cancel a series if the associated production and other hourly program costs continue to exceed the net advertising revenues and, especially, if the show demonstrates little prospect for improvement); Dominick & Pearce, *Trends in Network Prime-Time Programming 1953-74*, 26 J. COMM. 70 (Winter 1976). *See generally* EASTMAN, *supra* note 31, at 129-30.

37. In recent years, some commentators argue that the Act intended the FCC to do nothing more than coordinate broadcast operations so as to avoid electrical interference. They argue that no grounds exist for denying the electronic media the same First Amendment protection afforded to the print media and reject the theory that the scarcity of this public resource warrants governmental scrutiny of broadcast operations. *See, e.g.*, Mayron, *The Illegitimacy of the Public Interest Standard at the FCC*, 38 EMORY L.J. 715 (1989). Legislative history is contrary to these new claims. *See* F. KAHN, *supra* note 10, at 412-16. Long-unchallenged court rulings on this point also are contrary. *See, e.g.*, Red Lion Broadcasting Co. v. FCC, 396 U.S. 367, 388 (1969) (although broadcasting is a medium affected by a First Amendment interest, "[w]here there are substantially more individuals who want to broadcast than there are frequencies to allocate, it is idle to posit an unbridgeable First Amendment right to broadcast comparable to the right of every individual to speak, write or publish"); NBC v. United States, 319 U.S. 190, 215-16 (1943) (the Court rejected the argument that the

may seem to suggest that to the extent that the two—audience interest (assuming that it can be discerned) and the public interest—conflict, audience interest as measured by these ratings should be ignored on the theory that the surveyed listener or viewer cannot value accurately and will reject a documentary or news program in favor of rock music or the situation comedy.

The idea that there should be some disinterested agent influencing program choices is not as un-American as it first appears, for it rests on the idea that broadcasting cannot be viewed merely as a commercial system that operates on its own (or in response to market forces). Indeed, it is the media that "serve[s] to mobilize support for the special interests that dominate the state and private activity," through its "choices, emphases, and omissions."[38] The media is "able to fix the premises of discourse, to decide what the general populace is allowed to see, hear, and think about."[39] And of equal concern is the media's encouragement and reinforcement of stereotypical and false images.[40] To be sure, this is not an argument in favor of a "Min-

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FCC was a mere "traffic officer, policing the wave lengths to prevent stations from interfering with each other" and found that "[t]he facilities of radio are limited and therefore precious; they cannot be left to wasteful use without detriment to the public interest . . ."). For a more recent ruling, see Metro Broadcasting Inc. v. FCC, 110 S. Ct. 2997 (1990).

38. HERMAN & CHOMSKY, *supra* note 33, at xi.

39. *Id.* A recent study reported:

> A growing body of research evidence suggests that television plays an important role in socialization, especially for the young viewer. [Footnote omitted]. Social learning theory provides the dominant theoretical framework in accounting for television's socialization effects. [Footnote omitted]. Central to social learning is a focus on . . . behavioral actions of others. [Footnote omitted].
>
> . . . .
>
> . . . Television portrayals of behaviors and their causes may reflect, reinforce and/or influence people's implicit theories of social causality, thus warranting research attention.

Baxter & Kaplan, *Context Factors in the Analysis of Prosocial and Antisocial Behavior on Prime Time Television*, 27 J. BROADCASTING 25, 27 (1983). *See generally*, G. COMSTOCK, S. CHAFFEE, N. KATZMAN, M. MCCOMBS & D. ROBERTS, TELEVISION AND HUMAN BEHAVIOR (1978).

40. A. BANDURA, SOCIAL LEARNING THEORY (1977); D. CATER & S. STRICKLAND, T.V. VIOLENCE AND THE CHILD - THE EVOLUTION AND FATE OF THE SURGEON GENERAL'S REPORT (1975); Downs & Gowan, *Sex Differences in Reinforcement and Punishment on Prime-Time Television*, 6 SEX ROLES 683 (1980) ("One of the most influential factors in the development of children's sex-role stereotypes and behaviors is television"); Greenberg, CHILDREN'S REACTIONS TO TELEVISION BLACKS, 49 JOURNALISM Q. 5 (1972) (black and white youngsters identify with

istry of Information,"[41] but one to urge the employment of the power of the medium to the advantage and progress of our political society.

III. CHOOSING CONTENT IN THE PUBLIC INTEREST

The view that media corporations are privileged and should be encouraged to choose programs of some merit, beyond the simple entertainment value as would generate high ratings, is not just that of a lone disappointed television viewer. Even shareholders (whose economic interests in shows with high ratings, although of low merit, is obvious) have demanded higher standards. Most often, these demands take the form of shareholder proposals to be delivered at the corporations' annual meetings.[42] Not only have the efforts of these shareholders gone

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black television characters; white youngsters who watch blacks most on television are more likely to believe that real-life blacks are accurately portrayed).

41. *See* G. ORWELL, NINETEEN EIGHTY-FOUR (1949).

42. *See* CBS, SEC No-Action Letter, LEXIS 326 (1989); Capital Cities/ABC, Inc., SEC No-Action Letter, LEXIS 323 (1989); General Elec. Co., SEC No-Action Letter, LEXIS 304 (1989); Walt Disney Co., SEC No-Action Letter, LEXIS 1619 (1988).

Networks have long-maintained broadcast standards and practices departments that exercise total authority over all network programming. *See* EASTMAN, *supra* note 31, at 142. These departments "often find [themselves] walking a thin line between offending viewers or advertisers and destroying imaginative programming that may pull in high ratings." *Id.* On the whole however, the editorial power of these censors has been limited. For example, one department recently confronted the question of whether to censor bikini briefs in favor of boxer shorts. *Id.* In recent years, all three networks have significantly reduced the staffs of these departments, but not without protest from viewers and shareholders.

One CBS shareholder stated:

> The need for . . . self-policing by the networks is obvious. Viewers are concerned about the portrayal of sex, and violence, drug use and other anti-social conduct on T.V. They resent misleading and tasteless commercials.
> . . . .
> Broadcasters are required to serve the public interest. The public interest is not served by lowering standards and eviscerating the staff needed to enforce them. CBS is responding to competition by cheapening its product, not by improving quality. That is a questionable response from the point of view of its own interests, but it also clashes with the public interest.

CBS, SEC No-Action Letter, LEXIS 326, 6-7 (1989).

A group of General Electric shareholders argued that:

> The current trend in NBC broadcasting pattern shows a nearly total disregard for any understanding that the networks owe the public (or the Congress) a special duty of responsibility. Not only network programming, but also advertising contains excessive violence, indecent language, nudity, tolerant portrayals of drug use, semi-explicit sex, deviant perversions and other

largely uncelebrated by the media, they have been thwarted by a most formidable board position—that the nature, presentation and content of television programming is within the discretion of the corporation's managers. The board can assert this as a matter of general corporation law and also under federal securities laws.[43] To this extent, the board need not even communicate these shareholders' concerns to other shareholders, much less

> illegal conduct. The Company stands in violation of its own company standards!
>
> . . . .
>
> In quite a direct way our resolution puts before the Company management and the other shareholders the extraordinary question of how, exactly, the GE/NBC management is contending with the wide-spread degeneration in the area of decency. Cutting of standards staffs by GE/NBC and the disregarding of its own long-standing regulations appears to open the flood gates of national TV degradation, thereby desensitizing the public on a number of vital issues and promoting a kind of anti-social behavior that is certain to meet with resistance from individual Americans and American groups from every walk of life; not just from the so-called "right", but across the political spectrum.
>
> Flagrant disregard for the public welfare is certain to awaken the Congress to wonder why, if broadcasters no longer are required to meet a certain high standard to justify their use of a public monopoly on the electro-magnetic spectrum, they should be accorded its exclusive use through licensing.

General Elec. Co., SEC No-Action Letter, LEXIS 304, 5-6 (1989).

A group of Walt Disney shareholders proposed that:

> WHEREAS, U.S. television, film, and cable programs impact a worldwide audience with images reaching millions of women, men and youth, irrespective of racial, ethnic, economic group or sex, and this filmed programming is recognized as an important socialization influencing how persons view themselves and their world.
>
> WHEREAS, Minorities and women, and especially youth, are major viewers of film, television and cable programming and consumers of advertised products associated with these programs, but they are not significantly represented in the creative, managerial and professional decision-making positions in these industries;
>
> THEREFORE, BE IT RESOLVED that we shareholders request the Board of Directors of Walt Disney Company, Inc. to provide Affirmative Action reports . . . [to] include . . . [a] list of names and titles of all minorities and women working on film, television and cable programming who perform as: executive producers; producers; . . . writers; directors; . . . [a] description of approaches to better utilize the skills of minorities and women in the aforementioned programming development and production positions.

Walt Disney Co., SEC No-Action Letter, LEXIS 1619, 3 (1988).

43. Securities Exchange Act of 1934, General Rules and Regulations, 17 C.F.R. § 240.14a-8(c)(1), (7) (1990). Rule 14a-8 provides that where an eligible stockholder (i.e., one who is a record or beneficial owner of at least 1% or $1000 in market value of securities for at least one year) notifies the corporation of his intention to present a proposal for action at a forthcoming meeting of stockholders, the corporation must set forth the proposal in its proxy statement which it mails to the stockholders.

This provision is subject to thirteen exceptions, Rules 14a-8(c)(1) through (c)(13), consider anything besides the profitability of programs.[44]

The state of the law then is this: while the Act mandates service in the "public interest, convenience and necessity," the Commission requires nothing of broadcasters and only reacts in a negative fashion (through sanctions such as denial of renewal and fines) in the face of proven wrongdoing by licensees;[45] and while corporation law requires directors to manage the corporation so as to achieve maximum shareholder wealth, it also permits directors to indulge other non-shareholder interests.[46] This means that in this era of deregulation, corporate broadcasters can (but are not required to) assess program worth based on criteria other than audience ratings. But if they did, that is, if the directors of WCBS-TV declined to contract for "Uncle Buck"[47] because, like "Married . . . With Children," it is base and

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any one of which permits the corporation to omit the proposal. The two exceptions cited above provide:

> (1) If the proposal is, under the laws of the registrant's domicile, not a proper subject for action by security holders.
>
> Note: Whether a proposal is a proper subject for action by security holders will depend on the applicable state law. Under certain states' laws, a proposal that mandates certain action by the registrant's boards of directors may not be a proper subject matter for shareholder action, while a proposal recommending or requesting such action of the board may be proper under such state laws.
>
> . . . .
>
> (7) If the proposal deals with a matter relating to the conduct of the ordinary business operations . . . .

17 C.F.R. § 240.14a-8(c)(1), (7) (1990).

44. SEC No-Action Letters, *supra* note 42 (where the SEC decided to take no action on the boards' decisions to omit such shareholder proposals from the corporations' proxy materials.

45. Licensees are subject to penalties, for example, when they violate law or are dishonest with the FCC. *See* Policy Regarding Character Qualifications in Broadcast Licensing, 5 FCC Rcd 3252, 67 R.R.2d 1107 (1990); Policy Regarding Character Qualifications in Broadcast Licensing, 102 F.C.C.2d 1179, 59 R.R.2d 801, *reconsideration granted in part, denied in part,* 1 FCC Rcd 421, 61 R.R.2d 619 (1986), *appeal dismissed sub nom.* National Ass'n for Better Broadcasting v. FCC, No. 86-1179 (D.C. Cir. June 11, 1987), *modified,* 5 FCC Rcd 3252, 67 R.R.2d 1107 (1990). Licensees also are subject to penalties when they violate specific regulations. 47 U.S.C. § 307(d) (1988) (short renewal); 47 U.S.C. § 503(b) (1988) (fines for willful violations).

46. *See supra* note 26.

47. "Uncle Buck" is based on the movie of the same name. The main character is Buck Russell (John Candy in the film version), the "ne'er-do-well, coarse black sheep of the family," a "slob who eats constantly, smokes cigars," and "drives around in an incredibly noisy old boat of a car." VARIETY, Aug. 16, 1989, at 20 (Film Review). "Buck takes charge of his nephew and two nieces when their parents are suddenly

demeaning to women, the decision would be upheld as a valid exercise of the director's business judgment as a matter of corporate law. This issue of such managerial discretion is the subject of *Paramount Communications, Inc. v. Time, Inc.*

IV. Public and Private Interests in Board Decision Making

The main business of Time, Inc. is the publication of magazines and books. But Time has other substantial communications activities in pay television services through its subsidiaries, Home Box Office, Inc. and Cinemax, which deliver programs through cable systems nationwide, American Television and Communication Corporation, which owns several cable television franchises, and broadcast licensee, Turner Broadcasting System.[48] Time's executives began considering expansion beyond mere delivery of television programming into development and production in 1983. In 1987, a special committee of executives resolved to pursue such a plan on the basis of two considerations: Time's desire to have greater control over quality and price of the film products delivered through its cable network and franchises; and Time's concern over the increasing globalization of the world economy. Some of Time's outside directors, however, opposed this move as a threat to the editorial integrity and journalistic focus of Time, i.e., the "Time Culture." They believed that Time had become recognized in this country as an "institution built upon a foundation of journalistic integrity." In the board's view: "Time is an 'American institution' and has represented 'an enormous degree of integrity and honesty in trying to bring the news to the world.'. . . [It] has built a unique bond of trust with the American people."[49]

called out of town. The six and eight year old are precocious, wise-cracking kids with a colorful vocabulary." Travers, ROLLING STONE, Sept. 7, 1987, at 32 (Film Review).

48. The operation of cable systems is subject to regulation by the Federal Communications Policy Act of 1985, 47 U.S.C. § 521 (1990). Section 521 sets forth the purposes of the Federal Communications Policy Act, in particular to "establish franchise procedures and standards which encourage the growth and development of cable systems and which assure that cable systems are responsive to the needs and interests of the local community."

49. Time Defendants' Brief in Opposition to Plaintiffs' Motions for a Preliminary Injunction at 15-16, Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1989) (C.A. No. 10,866). This philosophy also controlled the operation of Time's cable business. *Id.*

It seemed that Time could achieve these goals best through a merger with a company already in the business of program production. Warner Brothers was its first choice.[50] When the first meeting with Warner Brothers[51] did not culminate in any agreement, Time considered other entertainment companies, including Disney, 20th Century Fox, Universal, and Paramount, although it continued talks with Warner Brothers. The Time board thought that a merger of Time and Warner was feasible only if: (1) a favorable stock-for-stock exchange could be negotiated; and (2) Time controlled the board of the resulting corporation in order to preserve a management committed to Time's journalistic integrity, i.e., the "Time Culture."[52]

After several months of further negotiations, the parties reached an agreement and approved the stock-for-stock merger in March 1989. The resulting company would have a 24-member board, with 12 members representing each corporation. The board would create an editorial committee with a majority of members representing Time. A similar entertainment committee would be controlled by Warner board members.

While Paramount seemed to have held ideas for the acquisition of Time, its disclosure surprised the business world.[53] As

50. Warner Brothers was in the business of the creation, production and distribution of films and programs for television and theaters. Defendant Warner Communications, Inc.'s Brief in Opposition To Plaintiffs' Motions for a Preliminary Injunction at 16-18, *Paramount Communications, Inc.*, 571 A.2d 1140 (C.A. No. 10,866).

51. Time and Warner Brothers discussed the possibility of a joint venture between the two companies through the creation of a jointly-owned cable company. Time would contribute its cable system and HBO. Warner would contribute its cable system and provide access to its Warner Brothers Studio. The resulting venture would be a large, more efficient cable network which would produce and distribute its own movies on a worldwide basis. Ultimately, the parties abandoned this plan, determining that it was impractical for several reasons, chiefly because of tax considerations. *Paramount Communications, Inc.*, 571 A.2d at 1144-45.

52. Warner also insisted on a stock-for-stock exchange and sought to preserve "its shareholders' equity in the resulting corporation." *Id.* at 1145. While the parties agreed that a stock-for-stock exchange was the best course, talks broke down over corporate governance issues. Time wanted a co-CEO proposal by Warner to be temporary and for the Warner CEO to retire in five years. However, the Warner CEO: "[R]efused to set a time for his retirement and viewed Time's proposal as indicating a lack of confidence in his leadership. Warner considered it vital that their executives and creative staff not perceive Warner as selling out to Time." *Id.* Warner rejected Time's request for a guarantee that Time would dominate the CEO succession "as inconsistent with the concept of a Time-Warner merger 'of equals.'" *Id.* This impasse brought an end to negotiations.

53. Apparently, the suddenness of Paramount's offer was feigned, because its

the Time board was likely to resist these ideas, Paramount began its takeover attempt by a tender offer to purchase all outstanding shares of Time for $175 per share. The next day, the trading price of Time's stock leaped from $126 to $170 per share. Paramount later proposed a merger to the Time board. Not surprisingly, the Time board considered Paramount's offer inadequate and concluded that the proposed merger with Warner was best for the corporation. While Time refused to negotiate with Paramount, the Time board realized that Paramount could still prevail through the purchase of the Time stock from individual shareholders. The Time board took the position that because it was charged by statute with directing the corporation and ensuring its well-being, and these shareholders (many of whom were institutional investors) could not appreciate the long-term benefits of the Warner merger, but would succumb to the temptation of certain cash, Time must defend against the takeover—to protect Time's control over its own destiny, as well as the equally precious "Time Culture."[54]

Paramount raised the all-cash offer to $200 per share, but

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board had decided as early as March 1989 to move to acquire Time. Paramount, however, delayed announcement of its proposal "until Time had mailed to its stockholders its Time-Warner merger proposal along with the required proxy statements" in order to create maximum confusion to shareholders. *Id.* at 1147 n.8.

54. The Time board decided to recast its consolidation with Warner into an outright cash and securities acquisition of Warner by Time. This course would not require the approval of Time stockholders, but only board action. The restructured deal proposed that: "Time would make an immediate all-cash offer for 51% of Warner's outstanding stock at $70 per share"; Time would purchase the remaining 49% "at some later date for a mixture of cash and securities worth $70 per share"; "[t]o provide the funds required for its outright acquisition of Warner, Time would assume 7-10 billion dollars worth of debt, thus eliminating one of the principal transaction-related benefits of the original merger agreement"; and, finally, Time also agreed to pay and amortize a $9 billion payment to Warner for the goodwill of Warner. *Id.* at 1148.

Warner's response to this proposal is described as follows:

> Warner agreed, but insisted on certain terms. Warner sought a control premium and guarantees that the governance provisions [(i.e., that there would be co-CEO's, one from Time, one from Warner, for a period of years after the merger)] found in the original merger agreement would remain intact. Warner further sought agreements that . . . unless enjoined, Time would be legally bound to complete the transaction. Time's board agreed to these last measures only at the insistence of Warner. For its part, Time was assured of its ability to extend its efforts into production areas and international markets, all the while maintaining the Time identity and culture.

Id. at 1148-49.

the Time board rejected this offer on the same grounds. Paramount then filed an action seeking a preliminary injunction to halt Time's defensive maneuvers. While Paramount's narrow interests were undeniable, as a shareholder of Time, it had the right to insist that board decisionmaking accord with strict fiduciary standards designed to protect the corporation. Paramount argued that the Time board failed to adhere to these standards in responding to Paramount's offer. Thus, Time's decision to reject Paramount and enter into the revised merger agreement with Warner was not entitled to the benefit of the business judgment rule. Specifically, Paramount argued that the Time directors had abdicated their responsibilities to the Time shareholders in favor of the "Time Culture"—a term, created by management and adopted by the directors, that involved little more than the preservation and enhancement of Time senior management positions.[55]

The Delaware Supreme Court rejected Paramount's challenge and held that the decision did warrant the court's deference under the business judgment rule.[56] This rule is a presumption that in making decisions, the directors have acted on an informed basis, in good faith, and in the honest belief that the action taken is in the corporation's best interest.[57] Under it, directors will not be liable for and the courts will not interfere with, nor pass upon, the wisdom of the board's decisions.[58] And

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55. Reply Brief of Plaintiffs-Appellants Paramount Communications, Inc. and KDS Acquisition Corp. at 14-17, *Paramount Communications, Inc.*, 571 A.2d 1140 (No. 279); Plaintiffs' Reply Brief in Support of Their Motion For A Preliminary Injunction at 11 & 21, 571 A.2d 1140 (No. 279).

56. However, the court first addressed the issue of whether the company was "for sale," an event which would trigger special duties for the board. The court found that the restructured deal with Warner did not have the effect of putting the corporation up for sale, which would have required the board to choose the course that would maximize immediate shareholder value. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986). Instead, the court viewed the board's reaction to Paramount's hostile tender offer as only a defensive response to a perceived threat to the well-being of the corporation; it was not an abandonment of the corporation's strategic plans. Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1150-51 (Del. 1989).

57. Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985). The party challenging a board decision has the burden of rebutting the presumption that the board acted within its discretion under the business judgment rule by showing gross negligence, bad faith, breach of trust or other such wrongful conduct. *Id.*

58. *Id.*

so long as the decision can be attributed to any rational purpose, the court may only consider the process by which the board formulated its decision. Clearly, this rule makes sense in ordinary matters, such as a decision to contract, to open or close a division, or to pay dividends. The extraordinary case of the hostile takeover, however, offers reasons not to indulge the board of directors to the same extent. Indeed, the Delaware courts have wisely recognized that "where issues of corporate control are at stake, there exists the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders."[59] In such cases, there is reason to inquire whether a defensive posture is no more than an instance of board entrenchment.

This issue was formally addressed in *Unocal Corp. v. Mesa Petroleum Co.*[60] There, the Delaware Supreme Court established an intermediate form of judicial review to judge the conduct of an independent board of directors in addressing a pending takeover bid. In these circumstances, the board must meet an "enhanced duty" at the threshold before it receives the normal protections of the business judgment rule.[61] This is to say that while in ordinary matters, the business judgment rule is a presumption of good faith in favor of the board, in a hostile takeover attempt, the board must make an initial showing of good faith to earn the court's deference. The court adopted a two-pronged test:

> before the business judgment rule is applied to a board's adoption of a defensive measure, the burden will lie with the board to prove (a) reasonable grounds for believing that a danger to corporate policy and effectiveness existed; and (b) that the defensive measure adopted was reasonable in relation to the threat posed. [citation omitted] Directors satisfy the first part of th[is] . . . test by demonstrating good faith and reasonable investigation. [citations omitted].[62]

59. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1287 (Del. 1989).

60. 493 A.2d 946 (Del. 1985).

61. Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1152 (Del. 1989).

62. *Id.* The court explained further: "*Unocal* involved a two-tier, highly coercive tender offer. In such case, the threat is obvious: shareholders may be compelled to tender to avoid being treated adversely in the second stage of the transaction." *Id.* (Citation omitted).

V. Cognizable Business Interests

What is the nature of the "danger to corporate policy and effectiveness" that would give rise to the privilege (and perhaps duty) of the board to defend against an aggressor (and thus warrant judicial deference)? Paramount argued that the only legally cognizable danger is inadequate value as viewed objectively of the takeover company's bid. And since Paramount made an all-cash offer at well-above the then market price, there was no danger to corporate policy and effectiveness. Paramount asserted further that such "non-shareholder specific concerns,"[63] namely the "Time Culture" and this notion of journalistic integrity, did not amount to a corporate policy entitled to any recognition by the court. Besides, Paramount pointed out, even assuming the point for the moment, it too had integrity.[64]

To be sure, in the face of Paramount's challenge of the propriety of such a non-traditional view of the corporation's objective, the Time board labored to characterize the "Time Culture" as a legitimate corporate policy. Logically, the Time board asserted that there was a " 'direct relationship' between Time's integrity and value for its shareholders,"[65] and that it was " 'not simply culture for culture's sake' — Time's magazines earn more than a third of the profits earned by all U.S. magazines, and have 22% of the revenues (as opposed to 8% for the number two company)."[66] At the same time, the board candidly argued that the " 'Time Culture' importantly include[d] directors' concerns for the larger role of the enterprise in society."[67] As stated by the corporation's founder and reaffirmed by his son and director,

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63. *Id.* at 1149; *see also* Plaintiff's Opening Brief in Support of Motion for a Preliminary Injunction at 53, *Paramount Communications, Inc.*, 571 A.2d 1140 (C.A. No. 10,866).

64. The court stated:

> Paramount and the individual plaintiffs extrapolate a rule of law that an all-cash, all-shares offer with values reasonably in the range of acceptable price cannot pose any objective threat to a corporation or its shareholders. Thus, Paramount would have us hold that only if the value of Paramount's offer were determined to be clearly inferior to the value created by management's plan to merge with Warner could the offer be viewed—objectively—as a threat.

571 A.2d at 1152-53.

65. Time Defendants' Brief in Opposition to Plaintiffs' Motion for a Preliminary Injunction at 16, 571 A.2d 1140 (C.A. No. 10,866).

66. Answering Brief of Time Appellees at 8, 571 A.2d 1140 (No. 279).

67. *Id.* at 9.

Time is "an enterprise operated in the public interest."[68] Under this view, inadequate value was only one cognizable danger posed by Paramount.[69]

The Court agreed with Time that Paramount's construction of earlier chancery decisions was too narrow and rigid.[70] The court explained:

> *Unocal* is not intended as an abstract standard; neither is it a structured and mechanistic procedure of appraisal. Thus, we have said that directors may consider, when evaluating the threat posed by a takeover bid, the "inadequacy of the price offered, nature and timing of the offer, questions of illegality, the impact on 'constituencies' other than shareholders . . . the risk of nonconsummation, and the quality of securities being offered in the exchange." [71]

Accordingly, the court concluded:

> [T]he Time board reasonably determined that inadequate value was not the only legally cognizable threat that Paramount's all-cash, all-shares offer could present. Time's board concluded that Paramount's eleventh hour offer posed other threats. One concern was

68. Time Defendants' Brief in Opposition to Plaintiffs' Motions for a Preliminary Injunction at 34, 571 A.2d 1140 (C.A. 10,866).

69. Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1142 (Del. 1989). The court went on to find that the board made an informed decision, having fully investigated the matter. *Id.* at 1153-54. On the second part of the *Unocal* analysis, the court explained the board's burden as follows:

> The obvious requisite to determining the reasonableness of a defensive action is a clear identification of the nature of the threat. As the Chancellor correctly noted, this "requires an evaluation of the importance of the corporate objective threatened; alternative methods of protecting that objective; impacts of the 'defensive' action, and other relevant factors."

Id. at 1154 (citation omitted).

On the facts there, the court found that the defensive action taken was a reasonable response to the perceived threat—it was "not aimed at 'cramming down' on its shareholders a management-sponsored alternative, but rather had as its goal the carrying forward of a pre-existing transaction in an altered form." *Id.* at 1154-55. Further, the revised agreement "did not preclude Paramount from making an offer for the combined Time-Warner company or from changing the conditions of its offer so as not to make the offer dependent upon the nullification of the Time-Warner agreement." *Id.* at 1155.

70. *Id.* at 1153.

71. *Id.* (Citation omitted). The court stated further that:

> [T]he question of "long-term" versus "short-term" values is largely irrelevant because directors, generally, are obliged to charter [sic] a course for a corporation which is in its best interests without regard to a fixed investment horizon. Second, absent a limited set of circumstances as defined under *Revlon*, a board of directors, while always required to act in an informed manner, is not under *per se* duty to maximize shareholder value in the short term, even in the context of a takeover.

Id. at 1150.

> that Time shareholders might elect to tender into Paramount's cash offer in ignorance or a mistaken belief of the strategic benefit which a business combination with Warner might produce.[72]

Indeed, "the record attests to the zealousness of Time's executives, fully supported by their directors, in seeing to the preservation of Time's 'culture,' i.e., its perceived editorial integrity in journalism."[73]

CONCLUSION

Significantly, the Time board rejected a philosophy that was calculated to produce immediate shareholder wealth in favor of other intangible, non-shareholder specific ends, whose relationship with long-term economic benefit was at most tenuous. To champion the notion of the "Time Culture" at the economic expense of shareholders is almost revolutionary. However, it is not clear from the case (nor from the "other constituency" statutes[74]) to what extent and degree the board must show some

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72. *Id.* at 1153.

73. *Id.* at 1152.

74. Some commentators have criticized these statutes as unwise and unworkable. *See, e.g.*, Committee on Corporate Laws, *Other Constituencies Statutes: Potential for Confusion*, 45 BUS. LAW. 2253 (1990); Hanks, *Non-Stockholder Constituency Statutes: An Idea Whose Time Should Never Have Come*, 3 INSIGHTS No. 3, at 20 (Dec. 1989).

The ABA Committee on Corporate Laws states:

> Other constituency statutes have typically been adopted as one measure, among others, designed to assist directors in forestalling unwanted takeovers. However, they address a question that is of much broader significance in corporate law and to society in general: whose interests should a corporation serve? The issues posed by this question are:
> (1) whether the corporation has some responsibility to employees, communities, and the others enumerated in other constituency statutes; (2) if so, how these thus far legally unenforceable responsibilities (except when they are created by contract, e.g., employment agreements, or specific statute, e.g., laws imposing environmental obligations) are to be meshed with the legally enforceable obligations of directors to shareholders; and (3) whether the board of directors should have the power or the duty to prefer the interests of those constituencies over the interests of shareholders in some circumstances.
>
> . . . .
>
> . . . The Committee believes that if the existing law is to be changed, however, it should be done only after a thoughtful, national debate dealing with the many and profound consequences of such a change, not by means of ambiguous statutory enactments adopted to deal with the hostile takeover phenomenon perhaps without consideration of their operation in other contexts.

Other Constituencies Statues, *supra*, at 2253-54.

relationship between any non-shareholder constituency considered and the long-term economic interests of the shareholders.[75] None should be required, particularly in the case of regulated

75. One author has stated that after the *Paramount Communications* case that:

> [I]n the context of reviewing decisions relating to the daily management of the company there is no difference between the statutes and the Delaware formulation of the business judgment rule. Director action in the best interest of the corporation will satisfy both the statutes and the rule; action not in the best interest of the corporation will satisfy neither.

Wallman, *Corporate Constituency Statutes: Placing the Corporation's Interests First*, Vol. 11, No. 2 BUS. LAW. UPDATE, 1, 2 (Nov./Dec. 1990). The author asserts that the arguments opposing these other constituency statutes are largely unfounded because:

> *First*, the statutes do *not* say the directors can take any action they wish provided it benefits some stakeholder group. The statutes *do* say the directors must act in the best interests of the corporation and, in so doing, may consider the interests of the corporation's constituencies.
>
> . . . .
>
> *Second*, the statutes (except one) are explicitly permissive. Apart from the traditional shareholder derivative action, they do not afford standing to sue to any stakeholder group.
>
> *Third*, the statutes create no "accountability" problem. . . . [F]or day-to-day matters, the statutes and the business judgment rule standards (at least after *Time*) essentially coincide. . . .
>
> *Finally*, as to the complaint that there has been insufficient debate, one can only wonder. The debate has now occurred in over half the states, has been the subject of law review commentary since the 1930s, and has been at the forefront of litigation in connection with takeovers for decades. How much more debate is required before legislatures are entitled to act?

Id.

On the other hand, Wallman argues that the benefits obtained from these statutes are many, being:

> *First*, they halt the trend toward the myopic view that the goal of corporate governance principles is to ensure that directors maximize shareholder value as reflected in current stock prices. Consequently, the statutes enhance the ability of directors to focus on long-term corporate strategies.
>
> *Second*, these statutes reject the principle—still embodied in Delaware law under *Revlon*—that the directors are *required* to engage in wealth transfers from stakeholders to shareholders in connection with the sale of the company. For example, in a number of transactions, shareholders have gained directly at the expense of bondholders, employees, and others. Bondholders may now protect themselves through indenture provisions but employees cannot. There is no merit to a mechanical legal rule that *requires* unfair wealth transfers.
>
> *Finally*, these statutes simply represent a better way of doing business. Our most formidable foreign competitors—Japan and Germany—have corporate cultures, laws, and governance principles embracing the corporate constituency concept to a greater degree than that contemplated by any of the state statutes. These statutes and the constituency concept they embody, far from being impediments to the creation of world class corporate competitors, may well be fundamental ingredients to the creation of such competitors. Even if some major institutional investors and financial press can't see

media corporations which control the marketplace of ideas, like Time, but also like CBS and NBC.

As the examples given here show, the existing regulatory structure is so sparse that "public interest" under it is only a faint hope. But this is no reason why such a concern cannot be self-imposed by corporations, based upon a self-assessment of role in society. Corporations already wield tremendous influence in the shaping of ideas, in defining goals and values. The boards of these corporations have the latitude to adopt programming strategies that appeal to our higher, as well as our humorous, instincts. As part of their normal decisionmaking, corporate broadcasters should be informed of the desirability, effects and value of programs as gleaned not just from ratings, but from diverse sources of information, and corporate broadcasters should be cognizant of not only the importance of entertaining, but also of the responsibility of enriching.

this, the corporate world can. In Pennsylvania, 90% of the companies subject to the new corporate constituency law chose to remain under the law. *Id.*